Report

of the

Examination of

Northern Finnish Mutual Insurance Company

Marengo, WI

As of December 31, 2001

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State of Wisconsin / OFFICE OF THE COMMISSIONER OF INSURANCE

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June 26, 2002

Honorable Connie L. O'Connell
Commissioner of Insurance
State of Wisconsin
121 East Wilson Street
Madison, Wisconsin 53702

Commissioner:

In accordance with your instructions, an examination has been performed as of December 31, 2001, of the affairs and financial condition of

NORTHERN FINNISH MUTUAL INSURANCE COMPANY
MARENGO, WI

and the following report thereon is respectfully submitted:

I. INTRODUCTION

The last examination of this company was made in 1998 as of December 31, 1997. The current examination covered the intervening time period ending December 31, 2001, and included a review of such subsequent transactions deemed essential to complete this examination.

The Summary of Examination Results contains elaboration on all areas of the company's operations. Special attention was given to the action taken by the company to satisfy the recommendations and comments made in the previous examination report.

The company was originally organized as a town mutual insurance company on November 14, 1914, under the provisions of the then existing Wisconsin Statutes. The original name of the company was Northern Wisconsin Finnish Farmers Mutual Town Fire Insurance Company. Subsequent amendments to the company's articles and bylaws changed the company's name to that presently used.

During the period under examination, there was one amendment to the articles of incorporation in 1999, and there was no amendment to the bylaws.

The new amendment was added to divide the managerial position into two separate co-manager positions. Also, the new amendment permits the board of directors to assign the duties of the secretary and treasurer to the co-managers. The new amendment was effective May 1, 1999.

A review of the certificate of authority revealed that the company is currently licensed to write business in the following counties:

Ashland, Bayfield, Douglas and Iron

The company is currently licensed to write property, including windstorm and hail, and nonproperty insurance.

A review was made of the policy and application forms currently used by the company. The company issues an approved policy with or without endorsements on a payment term basis of one year or less with premiums payable on the advanced premium basis. Policy fees charged policyholders are retained by the company.

Business of the company is acquired through eleven agents, three of whom are directors of the company. Agents are presently compensated for their services as follows:

Type of Policy	Compensation
Fire	11.75%
Wind/Hail	11.75%
Non-property	11.75%
Commercial	11.75%

Company agents perform the initial adjusting on most loss claims, and participate in the adjustment of smaller claims, but they do not have authority to perform final adjudication for any losses in any loss amount. Preliminary loss documentation is prepared by the agents and is then sent to the company office for review by the company's management. For a large claim, an independent claim adjuster will be hired, and receives $45.00 per hour for each loss adjusted plus $0.45 per mile for travel allowance.

Policyholders may participate in the management and control of the company by attending and voting at all annual or special meetings of the members. No member may vote by proxy. The annual meeting of the company for the election of directors and special meetings of the company are held in accordance with its articles of incorporation.

Board of Directors

The board of directors consists of nine members divided into three classes. One class is elected at each annual meeting for a term of three years. Vacancies on the board may be filled by the directors for the interim to the next annual meeting when a director shall be chosen for the unexpired term.

The current board of directors consists of the following policyholders of the company:

Name	Principal Occupation	Residence	Expiry
Matthew Granger	Building Contractor	Ashland, WI	2002
*Janice M. Penn	Nurse Practitioner /Insurance Agent	HighBridge, WI	2002
Thomas A. Riemer	Building Contractor	Ashland, WI	2002
*Elizabeth B. Campbell	Realtor/Insurance Agent	Iron River, WI	2003
M. James Nortunen	Farmer	Marengo, WI	2003
Lyle Thewis	Farmer	Mellen, WI	2003
*John Bonk	Retired Teacher/Insurance Agent	GrandView, WI	2004
Myron Ollanketo	Truck Driver	Marengo, WI	2004
Lelyn Stadnyk	Farmer	Ashland, WI	2004

Directors who are also agents are identified with an asterisk.

Members of the board currently receive $60 for each meeting attended and IRS standard mileage rate for travel expenses.

Officers

Officers are elected by the board of directors from among its members and hold office for one year or until their successors are duly elected and qualified.

Officers serving at the present time are as follows:

Name	Office	2001 Salary
Janice M.Penn	President	$ 1,200
Lyle Thewis	Vice President	$ 600
Elizabeth Campbell	Secretary / Treasurer	$ 0
Katherine Beach	Co-Manager	$31,110
Deborah J Schutte	Financial Co-Manager	$36,720

Company office management duties are performed by co-managers of the company, Katherine Beach and Deborah Schutte; they are currently employed pursuant to a written two-year co-management contract.

Committees of the Board

The company's bylaws allow for the formation of certain committees by the board of directors. The committees at the time of the examination are listed below:

Adjusting Committee (Inactive)
John Bonk
Mattew Granger
Myron Ollanketo
Janice Penn
Thomas Riemer

Executive Committee
Elizabeth Campbell
James Nortunen
Janice Penn (Chair)
Thomas Riemer
Lyle Thewis

Underwriting Committee (Inactive)
Elizabeth Campbell
Matt Granger
Myron Ollanketo
Thomas Riemer (Chair)
Lelyn Stadnyk

Personnel Committee
James Nortunen
Myron Ollanketo
Janice Penn (Chair)
Lyle Thewis

It was noted during the field exam that both the loss adjusting committee and the underwriting committee were inactive for more than one year, the last meeting held by the loss adjusting committee was on November 17, 2000, and the last meeting held by the underwriting committee was on January 24, 2000. The company established the Criteria Committee in May 2002, which was a special committee set up to implement a better underwriting guideline for categorizing the company's homeowner policies in the proper rate categories. At the June 17th 2002 board meeting, the board decided to reinitiate the adjusting committee and underwriting committee. Starting January 1, 2003, the committees will meet at least three times a year.

Growth of Company

The growth of the company during the past five years as compiled from its filed annual statements was as follows:

Year	Net Premiums Earned	Net Losses and LAE Incurred	Policies In Force	Net Income	Admitted Assets	Policyholders' Surplus
1997	$510,775	$325,249	2,390	$(22,140)	$1,021,948	$412,986
1998	495,910	313,368	2,319	(14,597)	979,119	409,472
1999	652,334	295,292	2,243	126,004	811,554	506,156
2000	582,349	472,167	2,162	(125,012)	766,820	441,322
2001	549,475	326,767	2,058	(44,954)	700,816	384,945

The ratios of premiums written, gross and net, to surplus as regards policyholders during the past five years were as follows:

Year	Gross Premiums Written	Net Premiums Written	Ending Surplus	Writings Ratios Gross	Writings Ratios Net
1997	$897,928	$525,613	$412,986	217%	127%
1998	885,116	498,181	409,472	216	122
1999	752,026	445,570	506,156	149	88
2000	865,696	558,862	441,322	196	127
2001	904,518	572,234	384,945	235	149

For the same period, the company's operating ratios were as follows:

Year	Net Losses and LAE Incurred	Other Underwriting Expenses Incurred	Net Earned Premiums	Loss Ratio	Expense Ratio	Composite Ratio
1997	$325,249	$231,904	$510,775	64%	44%	108%
1998	313,368	254,471	495,910	63	51	114
1999	295,292	251,710	652,334	45	56	102
2000	472,167	246,547	582,349	81	44	125
2001	326,767	269,619	549,475	59	47	107

During the past five years, gross premium written has increased slightly from $897,928 in 1997 to $904,518; net admitted assets decreased by 31% to $700,816, surplus decreased by 7% to $384,945. The company's last underwriting gain and net gain were in 1995 and 1999, respectively. The company experienced high net losses and LAE in 1998 and 2000 due to weather related losses. Besides an increase in claim severity, insufficient rates have also limited the company's ability to attain profitable operations.

II. REINSURANCE

The examiners' review of the company's reinsurance portfolio revealed that there is currently one ceding treaty. The treaty contained a proper insolvency clause and complied with s. Ins 13.09 (3), Wis. Adm. Code, concerning maximum wind loss. Company retentions of risk complied with s. Ins 13.06, Wis. Adm. Code.

Reinsurer:	Wisconsin Reinsurance Corporation
Effective date:	January 1, 2001
Termination provisions:	By either party at any January 1 anniversary date, by providing to the other party at least 90 days' advance written notice.

The coverages provided under this treaty are summarized as follows:

1.	Type of contract:	Class A Liability Reinsurance
	Lines reinsured:	All casualty business written by the company
	Company's retention:	$750 each and every loss occurrence
	Coverage:	100% excess of $750 each and every loss occurrence.
	Reinsurance premium:	For each annual period, 75% of the premium for each and every subject policy issued by the company. Premium ceded is fully earned by the reinsurer, and the reinsurer carries no unearned premium reserve under the contract.
2.	Type of contract:	Class B First Surplus Reinsurance
	Lines reinsured:	All property business written by the company
	Company's retention:	When the company's net retention is $200,000 or more in respect to a risk, the company may cede on a pro rata basis up to $800,000 of risk. When the company's net retention is $200,000 or less in respect to a risk, the company may cede on a pro rata basis up to 50% of such risk. The company shall retain an annual deductible amount equal to 10% of the loss and LAE otherwise recoverable under this contract.
	Coverage:	Pro rata portion of loss up to $800,000 in excess of $200,000 when reinsured risk is equal to or greater than $200,000. Coverage is the 50% pro rata portion of ceded risk when the risk is equal to or less than $200,000. The company's annual aggregate deductible is applicable to the recovery of amounts covered by the agreement.
	Reinsurance premium:	The pro rata portion of all premiums, fees and assessment charged by the company corresponding to the risks ceded under the agreement.

	Ceding commission:	Provisional commission allowed of 15% of premiums paid to the reinsurer, to be increased by 1% for each 1% decrease in the loss ratio below 65%, subject to a maximum commission rate of 35% when the loss ratio is 45% or less. Any amount above 65% loss ratio shall be considered a deficit, and shall be carried forward.
3.	Type of contract:	Class C-1 Excess of Loss Reinsurance First Layer
	Lines reinsured:	All property business written by the company
	Company's retention:	\$20,000 each and every risk resulting from one loss occurrence. The company shall also retain as an annual deductible an amount equal to \$20,000 or loss that would otherwise be recoverable under the contract.
	Coverage:	\$40,000 excess of \$20,000 each and every risk resulting from one loss occurrence.
	Reinsurance premium:	For each annual period, premium calculated as the sum of the immediately preceding four years losses incurred (paid and unpaid) multiplied by 125% of the net premium written during the same period. The rate for the current annual period of the contract is 19.45%. The company shall pay a deposit premium of \$147,600 payable in equal monthly installments of \$12,300. The minimum premium is \$118,080.
4.	Type of contract:	Class C-2 Excess of Loss Reinsurance Second Layer
	Lines reinsured:	All property business written by the company
	Company's retention:	\$60,000 each and every risk resulting from one loss occurrence.
	Coverage:	100% of any loss excluding LAE in excess of \$60,000 each and every risk resulting from one loss occurrence, to the reinsurer's limit of liability of \$140,000.
	Reinsurance premium:	For each annual period, premium calculated as 3.25% of current net premiums written in respect to the covered business. The company shall pay annual deposit premium of \$24,600 payable in equal monthly installments of \$2,050.
5.	Type of contract:	Class D/E Stop Loss Reinsurance
	Lines reinsured:	All business written by the company
	Company's retention:	For each annual period, an amount equal to 75% of the company's net written premiums.
	Coverage:	100% of the amount of aggregate annual losses that exceed 75% of the company's net written premiums during the corresponding annual period.
	Reinsurance premium:	For each annual period, an amount calculated based on the sum of losses incurred in the immediately preceding 8 years multiplied by 125% of net premiums written in the same period. Annual premium subject to the maximum rate of 25% of current net written premiums, minimum rate of 6.5% of current net written premiums. The rate for the current annual period of the contract is 6.5%.

III. FINANCIAL DATA

The following financial statements were filed with the Commissioner of Insurance in the company's annual statement at December 31, 2001. Adjustments made as a result of the examination are noted at the end of this section in the area captioned "Reconciliation of Policyholders' Surplus."

Northern Finnish Mutual Insurance Company
Statement of Assets and Liabilities
As of December 31, 2001

Assets	Ledger	Nonledger	Not Admitted	Net Admitted
Cash in Company's Office	$ 150	$	$	$ 150
Cash Deposited in Checking Account	20,664			20,664
Cash Deposited at Interest	154,634			154,634
Bonds (at Amortized Cost)	2,253			2,253
Stocks or Mutual Fund Investments (at Market)	444,197			444,197
Real Estate (Net of Accumulated Depreciation and Encumbrances)	73,937			73,937
Premiums, Agents' Balances, and Installments Booked but Deferred and Not Yet Due	1,306			1,306
Investment Income Due or Accrued	232			232
Electronic Data Processing Equipment – Excluding Software (Cost Less Accumulated Depreciation)	3,443			3,443
Other Assets: Furniture and Fixtures	3,985		3,985	
TOTALS	$704,801	$	$3,985	$700,816

Liabilities and Surplus

Net Unpaid Losses	$ 30,583
Unpaid Loss Adjustment Expenses	625
Commissions Payable	149
Fire Department Dues Payable	1,341
Unearned Premiums	258,901
Reinsurance Payable	2,996
Other Liabilities:	
Expense Related	
Accounts Payable	486
Nonexpense Related	
Pemiums received in advance	20,790
TOTAL LIABILITIES	315,871
Policyholders' Surplus	384,945
TOTAL	$700,816

Northern Finnish Mutual Insurance Company
Statement of Operations
For the Year 2001

Net Premiums and Assessments Earned	$549,475
Deduct:	
Net Losses Incurred	277,772
Net Loss Adjustment Expenses Incurred	48,995
Other Underwriting Expenses Incurred	269,619
Total Losses and Expenses Incurred	596,386
Net Underwriting Gain (Loss)	(46,911)
Net Investment Income:	
Net Investment Income Earned	1,518
Net Realized Capital Gains	52
Total Investment Income	1,570
Other Income:	
Miscellaneous Income	387
Total Other Income	387
Net Income (Loss) Before Policyholder Dividends and Before Federal Income Taxes	(44,954)
Net Income (Loss) Before Federal Income Taxes	(44,954)
Net Income (Loss)	$(44,954)

Northern Finnish Mutual Insurance Company
Reconciliation and Analysis of Surplus as Regards Policyholders
For the Five-Year Period Ending December 31, 2001

The following schedule is a reconciliation of surplus as regards policyholders during the period under examination as reported by the company in its filed annual statements:

	1997	1998	1999	2000	2001
Surplus, beginning of year	$410,777	$412,986	$409,471	$506,156	$441,322
Net income	(22,140)	(14,597)	126,004	(125,012)	(44,954)
Net unrealized capital gains or (losses)	24,637	9,301	(26,692)	57,872	(13,721)
Change in non-admitted assets	(288)	1,781	(2,627)	2,306	2,298
Surplus, end of year	$412,986	$409,471	$506,156	$441,322	$384,945

Reconciliation of Policyholders' Surplus

The examination resulted in no adjustments to policyholders’ surplus. The amount reported by the company as of December 31, 2001 is accepted.

IV. SUMMARY OF EXAMINATION RESULTS

Compliance with Prior Examination Report Recommendations

Comments and recommendations contained in the last examination report and the action taken on them by the company are as follows:

1. Business Plan—It is recommended that the company conduct a comprehensive review of its insurance policy pricing, and perform an intermediate-term historical analysis over the past 5 to 10 years of premiums and losses by lines of business. It is further recommended that the company perform a formal comparative analysis of its pricing relative to that of its significant competitors, and that the company adjust its rates where practicable on lines where the company is charging inadequate premium practicable on lines where the company is charging inadequate premium relative to the risks being underwritten and the rates charged by competitors.

   Action—Partial comliance, further comment is contained in the summary of current examination results.

2. Disaster Recovey Plan—It is recommended that the company establish a disaster recovery plan and provide for emergency resources commensurate with the company's business continuation requirements.

   Action—Compliance.

3. Custody of Invested Assets—It is again recommended that the company require the signature of at least two officers, directors, or employees for access to the company's bank safe deposit box, in conformity with Ins. 13.05 (4)(f), Wis. Adm. Code.

   Action—Compliance.

4. Custody of Invested Assets —It is recommended that the company maintain its assets in the name of the company or under the custody of an acceptable custodial arrangement with a qualified bank or banking and trust company, in compliance with s.610.23, Wis. Stat., and s. Ins 13.05(4)(f), Wis. Adm. Code.

   Action—Compliance.

5. Investment Rule Transition—It is recommended that the company acquire no additional Type 2 investments, and discontinue reinvesting Type 2 dividends in additional shares of Type 2 investments, until the company meets the required amount of Type 1 investments, pursuant to s. Ins 6.20 (6)(c) Wis. Adm. Code..

   Action—Compliance.

6. Uneared Premiums—It is recommended that the company retain copies of its year end reports reflecting policy register data, in compliance with the records retention requirements provided by s. Ins 6.80, Wis. Adm. Code.

   Action—Partial compliance, further comment is contained in the summary of current examination results.

Current Examination Results

Corporate Records

The minutes of the annual meetings of policyholders and meetings of the board of directors and any committees thereof, were reviewed for the period under examination and also for the subsequent current period.

Biographical data relating to company officers and directors have been reported in accordance with the provisions of s. Ins 6.52, Wis. Adm. Code.

The company has executed formal written agreements with its agents. The contracts include language indicating the agent will represent the company's interests "in good faith."

Business Plan

Compliance was reviewed in respect to a prior examination recommendation stating that the company develops a comprehensive business plan that addresses a number of issues. These issues include the following: 1) conducting a comprehensive review of its insurance policy pricing, 2) perform an intermediate-term historical analysis over the past 5 to 10 years of premiums and losses by lines of business, 3) perform a formal comparative analysis of its pricing relative to that of its significant competitors, and 4) adjust rates where practicable on lines where the company is charging inadequate premium relative to the risks being underwritten and the rates charged by its competitors.

Currently the company's business plan includes adjusting its rates where they think it is necessary, however the changes are still not adequate compared to its competitors' rates. The current business plan did not address a number of the other issues covered in the prior recommendation. The company continues to record poor underwriting results and has incurred net losses four out of the last five years. It is necessary for the company to build on its present analytical tools to better evaluate its business in order to be profitable.

Therefore it is again recommended that the company conduct a comprehensive review of its insurance policy pricing. It is recommended that the company perform an analysis over the past 5 to 10 years of premiums and losses by lines of business. It is further recommended that the company perform a formal comparative analysis of its pricing relative to that of its significant competitors. It is recommended that the company adjust its rates where practicable on lines where the company is charging inadequate premium relative to the risks being underwritten and the rates charged by competitors.

Conflict of Interest

In accordance with a directive of the Commissioner of Insurance, each company is required to establish a procedure for the disclosure to its board of directors of any material interest or affiliation on the part of its officers, directors, or key employees which conflicts or is likely to conflict with the official duties of such person. A part of this procedure is the annual completion of a conflict of interest questionnaire by the appropriate persons. The company has adopted such a procedure for disclosing potential conflicts of interest. Conflict of interest questionnaires were reviewed for the period under examination with no apparent conflicts being noted.

The review of conflict of interest questionnaires revealed that three directors did not disclose the fact that they are also agents for the company (and also for another insurance company) as a potential conflict of interest. Directors of the company who are agents have a potential conflict of interest that should be formally disclosed to the other directors in compliance with s. 612.18, Wis. Stat. It is recommended that directors who are agents for the company disclose this as a potential conflict in their annual conflict of interest questionnaires. When a director has a material interest in a transaction involving the company, it is recommended that the director abstain from voting on the item, and the company should report the transaction to this office immediately, pursuant to s. 612.18 and 611.60, Wis. Stat.

Fidelity Bond and Other Insurance

The company is afforded coverage under the terms of the following bonds or contracts and has complied with s. Ins 13.05 (6), Wis. Adm. Code, which sets forth the minimum requirements for fidelity bond coverage:

Type of Coverage	Coverage Limits
Fidelity Bond	$ 70,000
Professional liability	1,000,000 each claim/aggregate limit
Directors and officers liability	1,000,000 each claim/aggregate limit
Insurance agents errors and omissions:	1,000,000 each claim/aggregate limit
Property:	
Building	180,000
Worker’s compensation	Wisconsin requirements
Employers liability:	
Bodily injury by accident	100,000 each accident
Bodily injury by disease	500,000 policy limit
Bodily injury by disease	100,000 each employee

Underwriting

The company has a written underwriting guide. The guide, which is currently under revision, covers all the lines of business that the company is presently writing. Currently the company's underwriting guide does not include specific guidelines to follow that clearly defines each of class of business under broader individual categorized lines of business. This allows agents too much discretion when categorizing and pricing a policyholder's risk. The company may run into cases where a substandard risk will receive a preferred rate, which leads to inadequate pricing. Therefore it is recommended that the company revise its underwriting guide to clearly specify, what risks qualify and do not qualify under each individual class of coverage offered by the company, which would eliminate agent discretion when pricing policyholder risks.

The company has a formal inspection procedure for both new and renewal business. However, the procedure, does not include inspection, on a sample basis, by underwriting committee members independent of the risk under consideration, as the underwriting committee has been inactive since January 2000. At the June 17, 2002 board meeting, the board decided to reactivate the underwriting committee starting in 2003. Therefore a sampling of new applications and of renewal business will be inspected by committee members independent of the risk under consideration. The underwriting committee will consist of at least three directors, and the committee will meet at least three times a year, starting January 2003.

Claims Adjusting

The company's adjusting committee has been inactive since November 2000. At the June 17^{th} board meeting, the board decided to reactivate the adjusting committee to supervise the adjustment of losses. The adjusting committee will consist of at least three directors, and the committee will meet at least three times a year, starting January 2003. However, the committee should meet as needed to resolve any claims that are outstanding and needs the attention of the adjusting committee so that claims are settled in a timely matter in accordance with s. 612.13(4), Wis. Stats. Therefore, it is recommended that the company's board appointed adjusting committee meet as needed to resolve any outstanding claims in a timely matter in accordance with s. 612.13(4), Wis. Stats.

Accounts and Records

The examiners' review of the company's records indicated that the company is in compliance with s. Ins 13.05, Wis. Adm. Code, which sets forth the minimum standards for the handling of cash and recording of cash transactions by town mutual insurance companies. The examiners noted the following:

1. A proper policy register is maintained
2. A proper cash receipts journal is maintained
3. A proper cash disbursements journal is maintained
4. A proper general journal is maintained
5. A proper general ledger is maintained

During the examination, the examiner noted that the company did not maintain a policy register for 2001. The company's current premium system was developed by an independent contractor. It was noted that the system could not readily generate the policy register which contains the policy number, premium amount, effective date of policy, term of policy and other related data. The company did not comply with s. Ins 6.80, Wis. Adm. Code, as regards to record retention. The recommendation may be found in the section titled "EDP Environment".

An extensive review was made of income and disbursement items. Cash receipts were traced from source records and the proper recording and eventual deposit thereof ascertained. Negotiated checks issued during the period under examination were reviewed, test checked for proper endorsement, and traced to cash records. Checks issued by the company require two signatures for any amount over $3,000. Checks are pre-numbered; both blank and voided checks are kept in the fireproof safe.

The verification of assets and determination of liabilities were made as of December 31, 2001.

The company is audited annually by an outside public accounting firm, in accordance with s. Ins 50.05 (1), Wis. Adm. Code.

EDP Environment

Company personnel were interviewed with respect to the company's Electronic Data Processing environment. Access to the computers is limited to people authorized to use the computers.

Company personnel back up the computers daily, and the backed-up data is kept off-site.

The company was unable to produce a hard or electronic copy of policy register record, as required by s. Ins 6.80, Wis. Adm. Code, which requires the company to retain records of its operations and other financial records reasonably related to insurance operations since the last OCI examination. If the company retained its year-end backed-up data, it would have been possible to recreate these reports. It is recommended that the company retain its year-end backed-up data for its policy register record for each year between OCI examinations, pursuant to s. Ins 6.80, Wis. Adm. Code.

A manual which describes how to use the company's software and outlines the steps to complete specific tasks assists in the continuity of operations for seldom-used applications, training, or when staff turnover occurs. The company has manuals documenting the use of its software.

Disaster Recovery Plan

A disaster recovery plan identifies steps to be performed in case the company loses a key employee, is not able to access its computer, information on its computer was lost, or the office building was destroyed, to name a few contingencies. The company has developed a disaster recovery plan.

The company's disaster recovery plan appears to be adequate.

Invested Assets

Section 610.23, Wis. Stat., requires insurers to hold all investments and deposits of its funds in its own name except that:

(1) Securities kept under a custodial agreement or trust arrangement with a bank or banking and trust company may be issued in the name of a nominee of the bank or banking and trust company; and

(2) Any insurer may acquire and hold securities in bearer form.

For securities not held under a custodial agreement or trust arrangement with a bank or banking and trust company, s. Ins 13.05 (4), Wis. Adm. Code, requires that:

> Non-negotiable evidences of company investments such as registered bonds, certificates of deposits, notes, etc., shall be maintained in a safe or vault with adequate safety controls or in a safety deposit box in a bank. Negotiable evidences of company investments shall be maintained in a safety deposit box in a bank. Access to a company safety deposit box containing negotiable securities shall require the presence and signature of at least 2 officers, directors or employees of the company.

The company is in compliance with these requirements.

Investment Rule Compliance

The investment rule for town mutuals allows a company to invest in common stocks, common stock mutual funds, and other higher risk investments (referred to as "Type 2") provided that the town mutual has a sufficient amount of lower risk investments (referred to as "Type 1"). A town mutual may invest in Type 2 securities only if it already has sufficient Type 1 investments. Type 1 investments must equal or exceed the greater of items 1, 2, or 3.

1.	Liabilities plus $300,000	$615,871
2.	Liabilities plus 33% of gross premiums written	614,362
3.	Liabilities plus 50% of net premiums written	601,988
4.	Amount required (greater of 1, 2, or 3)	615,871
5.	Amount of Type 1 investments as of 12/31/200	245,380
6.	Excess or (deficiency)	(370,491)

The company does not have sufficient Type 1 investments.

Company's current holding of Type 2 assets are the acquisition of mostly common and preferred stock that have been approved by this office, or were acquired prior to this office's investment rule.

Since the prior examination, the company did not make any additional Type 2 investments when there was a deficiency in Type 1 investments.

ASSETS

Cash and Invested Cash **$**175,448

The above asset is comprised of the following types of cash items:

Cash in company's office	$ 150
Cash deposited in banks-checking accounts	20,664
Cash deposited in banks at interest	154,634
Total	$175,448

Cash in the company's office at year-end represents the company's petty cash fund. A physical count was made by the examiners during the course of the examination and the balance reconciled to year-end.

Cash deposited in banks subject to the company's check and withdrawal consists of one account maintained in one bank. Verification of checking account balances was made by obtaining confirmations directly from the depository and reconciling the amounts shown thereon to company records.

Cash deposited in banks represents the aggregate of five deposits in four depositories. Deposits were verified by direct correspondence with the respective depositories and by an actual count and inspection of certificates and/or passbooks. Interest received during the year 2001 totaled $8,161 and was verified to company cash records. Rates of interest earned on cash deposits ranged from 2.23% to 7.3%. Accrued interest on cash deposits totaled $221 at year-end.

Book Value of Bonds **$**2,253

The above asset consists of the aggregate book value of bonds held by the company as of December 31, 2001. There is only one bond held by the company as of December 31, 2001. The bond investment was held in the custody of a securities broker.

The bond was subsequently disposed of prior to field exam. Bond purchases and sales for the period under examination were checked to brokers' invoices and advices. The company's investment in bonds was in conformance with Wisconsin Statutes and the rules of the Commissioner of Insurance as regards investments made by town mutual insurers.

Interest received during 2001 on bonds amounted to $170 and was traced to cash receipts records. Accrued interest of $11 at December 31, 2001, was checked and allowed as a nonledger asset.

Stocks and Mutual Fund Investments **$**444,197

The above asset consists of the aggregate market value of stocks and mutual funds held by the company as of December 31, 2001. Stocks owned by the company are located in the company's safety deposit box.

Stock certificates were physically examined by the examiners. Stock and mutual fund purchases and sales for the period under examination were checked to brokers' invoices and advices. The company's investment in stocks and mutual funds was in conformance with Wisconsin Statutes and the rules of the Commissioner of Insurance as regards investments made by town mutual insurers

Dividends received during 2001 on stocks and mutual funds amounted to $8,613 and were traced to cash receipts records. Accrued dividends of $183 at December 31, 2001, were checked and allowed as a nonledger asset.

Book Value of Real Estate **$**73,937

The above amount represents the company's investment in real estate as of December 31, 2001. The company's real estate holdings consists solely of its home office building purchased in 1991.

The required documents supporting the validity of this investment were reviewed and were in order. Adequate hazard insurance was carried on the real estate and contents as noted under the caption, "Fidelity Bond and Other Insurance." The company's investment in real estate and related items was in conformance with the Wisconsin Statutes and the rules of the Commissioner of Insurance as regards investments made by town mutual insurers. Real estate depreciation is calculated using the straight-line depreciation method.

Premiums in Course of Collection **$**1,306

The above ledger asset represents the amounts due from agents or policyholders which are not in excess of 90 days past due at year-end. A review of individual agent's accounts verified the accuracy of this asset.

Investment Income Due and Accrued **$**232

Interest due and accrued on the various assets of the company at December 31, 2001, consists of the following:

Cash at interest	$221
Bonds	11
Total	$232

Equipment, Furniture, and Supplies **$**3,985

This asset consists of $3,985 of office equipment and furniture owned by the company at December 31, 2001. In accordance with annual statement requirements, this amount has been deducted as an asset not admitted.

Electronic Data Processing Equipment **$**3,443

The above asset represents the company's computer equipment; net of accumulated depreciation thereon, excluding application software. Computer equipment is depreciated over a period of five years using the modified accelerated cost recovery system (MACRS) method. A review of the company's depreciation schedules ascertained the reasonableness of this balance.

LIABILITIES AND SURPLUS

Net Unpaid Losses **$**30,583

This liability represents losses incurred on or prior to December 31, 2001, and remaining unpaid as of that date. The examiners' development of unpaid losses is compared with the amount estimated by the company in the following schedule. Differences are reflected in the section of this report captioned "Reconciliation of Policyholders' Surplus."

	Company Estimate	Examiners' Development	Difference
Incurred But Unpaid Losses	$45,360	$50,518	$ 5,158
Less:			
Reinsurance Recoverable on Unpaid Losses	14,777	17,177	2,400
Net Unpaid Losses	$30,583	$33,341	$2,758

The examiners developed this liability by totaling actual loss payments made through the development period on those losses incurred on or prior to December 31, 2001. To the actual paid loss figures was added an estimated amount for those 2001 and prior losses remaining unpaid at the examination date, if any. Surplus is not adjusted for difference noted above, as the above difference of $2,758 was not considered material for purposes of this examination.

The examiners' review of claim files included open claims, paid claims, claims closed without payment, and all claims which were denied during the examination period. The review indicated that claims are investigated and evaluated properly and that payments are made promptly and in accordance with policy provisions upon the submission of a proper proof of loss. In addition, the review of claims handling procedures and files revealed the following:

1. A proper loss register is maintained.
2. Claim files contained sufficient investigatory data and documentation to verify settlement payments or reserve estimates.
3. Proofs of loss were properly signed.

Property claims are recorded in a loss register maintained by the company and the Liability claims are recorded in another loss register maintained by the company’s reinsurer. The company's reinsurer handles the adjustment of all liability losses. The company is provided with a report detailing the claim number, name of insured, policy number, claimant, loss date, loss payments, and outstanding direct and ceded loss reserves by accident year, by its reinsurer, Wisconsin Reinsurance Corporation. The two loss registers combined meet the requirements stated in s. Ins 13.05 (3) (f), Wis. Adm. Code, that all losses are to be recorded in a loss register that includes the report date and cause of loss, as well as the items listed above.

Unpaid Loss Adjustment Expenses **$**625

This liability represents the company's estimate of amounts necessary to settle losses which were incurred prior to December 31, 2001, but which remained unpaid as of year-end. The methodology used by the company in establishing this liability is management estimation of expense, the estimation is based on experience in prior years and the number of reported losses that remain open at the current year-end.

The examiners' analysis of expenses incurred in the current year related to the settlement of prior year losses, as well as estimates of amounts necessary to settle any prior losses remaining unpaid at the examination date, determined this liability to be adequately stated.

Unearned Premiums **$**258,901

This liability represents the reserve established for unearned premiums in compliance with s. Ins 13.08 (3), Wis. Adm. Code. This reserve was established using a daily pro rata methodology.

Reinsurance Payable **$**2,996

This liability consists of amounts due to the company's reinsurer at December 31, 2001, relating to transactions which occurred on or prior to that date.

Class A Liability adjusted premiums	$(1,204)
Class C C-1 Layer adjusted premiums	2,000
Class C C-2 Layer adjusted premiums	1,200
Class D/E Stop Loss adjusted premiums	1,000
Total Reinsurance Payable	$ 2,996

Subsequent cash disbursements and reinsurance accountings verified the amount of this liability.

Fire Department Dues Payable **$**1,341

This liability represents the fire department dues payable at December 31, 2001.

The examiners reviewed the company's fire department dues calculation and found this liability to be correctly calculated. The actual amount paid was verified to the cash disbursement records.

Commissions Payable **$**149

This liability represents commissions due agents on premium balances due and uncollected as of year-end. Supporting records and subsequent cash disbursements verified this item.

Accounts Payable **$**486

This liability represents an accrual for the miscellaneous unpaid office bills as of December 31, 2001, the examiner's subsequent search for unrecorded liabilities revealed additional liability of $103, the difference were considered immaterial, no adjustment to surplus was made.

Premium Received in Advance **$**20,790

This liability represents premiums paid on or before December 31, 2001 for the amount due on the next policy anniversary date. The examiner traced the balance to a detailed inventory of advance premiums, and verified a sample of advance premium by review of the policy files and cash receipts records.

V. CONCLUSION

The current examination resulted in no adjustments to surplus or reclassification; surplus as regards policyholders, per annual statement and examination, is $384,945.

The examination resulted in nine recommendations. Two of recommendations are similar to these from prior examination. Four recommendations relate to management and control, one recommendation relates to underwriting, one recommendation relates to claims adjusting, and the other recommendation relates to the company’s electronic data processing environment.

During the period under examination, the company has experienced a material decline in policyholders' surplus. Besides an increase in claim severity and a rise in the cost of reinsurance, insufficient policy pricing has been considered another major cause that limits the company's ability to attain profitable operations.

Management has taken steps to increase rate and deductibles, and implement a better underwriting guide. The board of directors also agreed to reactivate the claim adjusting committee and underwriting committee. Hopefully, these positive steps taken by the company will help the company improve its financial position and continue to serve its policyholders surrounding the Chequamegon Bay area of Lake Superior.

VI. SUMMARY OF COMMENTS AND RECOMMENDATIONS

1. Page 15 - Business Plan—Therefore it is again recommended that the company conduct a comprehensive review of its insurance policy pricing.

2. Page 15 - Business Plan—It is recommended that the company perform an analysis over the past 5 to 10 years of premiums and losses by lines of business.

3. Page 15 - Business Plan—It is further recommended that the company perform a formal comparative analysis of its pricing relative to that of its significant competitors.

4. Page 15 - Business Plan—It is recommended that the company adjust its rates where practicable on lines where the company is charging inadequate premium relative to the risks being underwritten and the rates charged by competitors

5. Page 16 - Conflict of Interest—It is recommended that directors who are agents for the company disclose this as a potential conflict in their annual conflict of interest questionnaires.

6. Page 16 - Conflict of Interest—When a director has a material interest in a transaction involving the company, It is recommended that the director abstain from voting on the item, and the company should report the transaction to this office immediately, pursuant to s. 612.18 and 611.60, Wis. Stat.

7. Page 17 - Underwriting—It is recommended that the company revise its underwriting guide to clearly specify, what risks qualify and do not qualify under individual class of coverage offered by the company, which would eliminate agent discretion when pricing policyholder risks.

8. Page 17 - Claims Adjusting—It is recommended that the company's board appointed adjusting committee meet as needed to resolve any outstanding claims in a timely matter in accordance with s. 612.13(4), Wis. Stats.

9. Page 19 - EDP Environment—It is recommended that the company retain its year-end backed-up data for its policy register record for each year between OCI examinations, pursuant to s. Ins 6.80, Wis. Adm. Code.

VII. ACKNOWLEDGMENT

The courteous cooperation extended to the examiners by the company's personnel is hereby acknowledged.

In addition to the undersigned, Christine Shan of the Office of the Commissioner of Insurance, State of Wisconsin, participated in the examination:

Respectfully submitted,

John Litweiler
Examiner-in-Charge